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Supreme Court, U.S.
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No. 03-1094

IN THE

Supreme Court of the United States

GENERAL MILLS, INC., ET AL.,
Petitioners,

v.

COMMISSIONER OF REVENUE,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE SUPREME JUDICIAL COURT OF THE
COMMONWEALTH OF MASSACHUSETTS

BRIEF IN OPPOSITION OF MASSACHUSETTS COMMISSIONER OF REVENUE

THOMAS F. REILLY
Attorney General
of Massachusetts

THOMAS A. BARNICO*
VICTORIA S. COLE
Assistant Attorneys General
One Ashburton Place, Room 2019
Boston, Massachusetts 02108
(617) 727-2200, ext. 2086
**Counsel of Record*

Questions Presented

1. Whether the Court has jurisdiction to review a decision of the Massachusetts Supreme Judicial Court where the federal constitutional questions presented to this Court were not raised or resolved below.

2. Whether the Massachusetts Commissioner of Revenue violated the due process and commerce clauses when he taxed a gain derived by The Talbots, Inc., a Massachusetts corporation, from what was deemed a sale by Talbots of its assets pursuant to an Internal Revenue Code § 338(h)(10) election.

3. Whether the Massachusetts Commissioner of Revenue violated the due process and commerce clauses when he taxed a sale of Talbots's intangibles after determining that Talbots, not a sham Delaware corporation, was the actual seller of the intangibles.

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Jurisdiction

Petitioners invoke 28 U.S.C. § 1257(a). However, the Court does not have jurisdiction over the questions presented because they were not actually decided by the Supreme Judicial Court or properly raised by Petitioners below.

Facts

For purposes of this Brief in Opposition to the Petition for a Writ of Certiorari, the Respondent Massachusetts Commissioner of Revenue ("Massachusetts Commissioner") accepts and incorporates by reference the facts set forth in the decision of the Supreme Judicial Court. *General Mills, Inc. v. Commissioner of Revenue*, 440 Mass. 154, 795 N.E.2d 552 (2003) (reproduced in the Appendix to the Petition for a Writ of Certiorari ("Pet. App.") at 1a-30a).

Some facts merit emphasis:

1. Petitioners General Mills, Inc. and The Talbots, Inc. (together, "Petitioners") dispute tax that the Massachusetts Commissioner imposed on Talbots, a former subsidiary of General Mills. Pet. App. 2a-3a. Until its sale in 1988, Talbots was a Massachusetts corporation with corporate headquarters in Hingham, Massachusetts, and extensive management and operational ties to Massachusetts. Pet. App. 5a, 28a-29a.

2. In 1988, following negotiations with Jusco Co., Ltd. ("JCL"), General Mills entered into an agreement with Jusco

(U.S.A.), Inc., a Delaware subsidiary of JCL, for the purchase and sale of Talbots. Pet. App. 7a. JCL, however, did not agree to a simple sale of stock. Pet. App. 7a-10a, 27a. Instead, JCL agreed both to buy assets directly and to structure a subsequent stock sale as an asset sale. Pet. App. 7a-10a, 27a. The parties structured their agreement as two separate transactions, involving four distinct corporations, occurring on different days. Pet. App. 7a-10a, 27a.

3. The first transaction, completed on June 26, 1988 ("Day 1"), was originally to be a sale by Talbots of its intangibles to Jusco (Europe), a JCL subsidiary in the Netherlands. Pet. App. 8a-9a. However, in response to General Mills's concern that the proposed sale would create a taxable dividend in Massachusetts, JCL proposed an alternative plan to eliminate any potential Massachusetts tax. Pet. App. 8a. Under the new plan, Talbots assigned its intangibles to the newly created Tal HC, Inc., a Talbots subsidiary incorporated in Delaware. Pet. App. 8a-9a. Then, on June 26, 1988, Tal HC sold the Talbots intangibles to Jusco (Europe) for $100 million. Pet. App. 9a. On its consolidated federal tax return, General Mills reported Tal HC's sale of Talbots's intangibles as a direct sale of assets by Tal HC. Pet. App. 10a. The Massachusetts Commissioner, after audit, determined that Tal HC was created solely to avoid Massachusetts tax. Pet. App. 3a. Accordingly, the Massachusetts Commissioner included the gain in Talbots's Massachusetts gross income and placed the receipts from the sale in the numerator of Talbots's Massachusetts sales factor. Pet. App. 3a, 28a.

4. The second transaction occurred on June 27, 1988 ("Day

2"), when General Mills sold its Talbots stock to Jusco (U.S.A.) for $325 million. Pet. App. 9a. Approximately nine months later, General Mills and Talbots joined Jusco (U.S.A.) in an election under Internal Revenue Code ("I.R.C.") § 338(h)(10) to treat the stock sale as a sale by Talbots of its remaining assets. Pet. App. 10a. The parties had agreed that General Mills would receive $3 million as consideration for joining with JCL in the election. Pet. App. 7a. General Mills's federal consolidated tax return and Massachusetts combined return both treated the sale of Talbots's stock as a sale of assets by Talbots. Pet. App. 10a. The election produced Massachusetts tax consequences consistent with the federal treatment of the gain. Pet. App. 23a. (Later, Petitioners filed an application for abatement with the Massachusetts Commissioner, alleging that Talbots had reported the income from the deemed asset sale in error. Pet. App. 2a-3a.)

Reasons for Denying the Writ

Petitioners ask this Court to review the questions whether the Massachusetts Commissioner violated the due process and commerce clauses when he (1) taxed the Day 1 sale of the Talbots intangibles by applying the step-transaction doctrine to conclude that Talbots, not a sham Delaware corporation, was the actual seller of the intangibles; and (2) taxed the gain Talbots derived, under the I.R.C. § 338(h)(10) election, from the deemed sale of its assets in the Day 2 transaction. Pet. 13-19. The Petition should be denied because the claims are not properly before this Court and in any event present no issues warranting this Court's review.

I. THE COURT LACKS JURISDICTION OVER PETITIONERS' CLAIMS BECAUSE THE QUESTIONS PRESENTED WERE NOT RAISED OR PASSED UPON BELOW.

The Petition should be denied because the two questions presented were not pressed or passed upon below. *See* Supreme Court Rule 14(g)(i) (petition for review of state court judgment must demonstrate that federal questions were "timely and properly raised" below); *McGoldrick v. Compagnie Generale*, 309 U.S. 430, 434 (1940) ("[i]n cases coming here from state courts there are reasons of peculiar force which should lead us to refrain from deciding questions not presented or decided in the highest court of the state"); Robert L. Stern *et al.*, *Supreme Court Practice* § 3.16, at 168-71 (8th ed. 2002) (collecting authorities). Accordingly, this Court lacks jurisdiction over Petitioners' claims under 28 U.S.C. § 1257.

The Supreme Judicial Court found that, while Petitioners had argued before the Massachusetts Appellate Tax Board that state

taxation on the I.R.C. § 338(h)(10) election violated the due process clause, they did not argue the issue on appeal, and thus it was waived under Massachusetts Rule of Appellate Procedure 16(a)(4). Pet. App. 18a n.7. *See Beck v. Washington*, 369 U.S. 541, 549-54 (1962) (constitutional claim must be pursued in the manner and with the degree of specificity required by the state rules of practice). In their Petition for Rehearing, the Petitioners insisted that they had argued due process and commerce clause claims on pages 8-9 and 18-19 of their appellate brief. Pet. App. 107a-108a. The Supreme Judicial Court denied the Petition for Rehearing, and rightly so. Pet. App. 84a. Pages 8-9, besides not containing the argument Petitioners now seek to present, are within the brief's Statement of Facts, not its Argument section. Nor is any argument on the constitutional claim found at pages 18-19, where, as Petitioners admitted in their Petition for Rehearing, they simply "noted" that the Massachusetts Appellate Tax Board had rejected any attempt to tax the sale of non-unitary subsidiaries. Pet. App. 107a. The brief then went on to argue the non-federal claim that the Supreme Judicial Court ultimately rejected: that the federal "fiction" of an I.R.C. § 338(h)(10) election should not control the calculation, under Massachusetts law, of gross income.

Also not raised or resolved below was Petitioners' other constitutional claim, regarding the application of the step-transaction doctrine to the Day 1 intangibles sale.[1] The Supreme Judicial Court

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[1] Petitioners did argue below that the effect of placing the receipts from the Day 1 sale of intangibles in the numerator of Talbots's Massachusetts sales factor together with only one month of regular sales from the relevant fiscal year distorted Talbots's actual business activity in Massachusetts and thereby resulted in an extraterritorial tax in violation of the due process and commerce

did not even comment on this constitutional claim, no doubt because the court was unaware that it was part of the case. Pet. App. 1a-30a. The claim was not argued to the Massachusetts Appellate Tax Board or articulated in Petitioners' brief to the Supreme Judicial Court. Rather, Petitioners contended below that Tal HC, not Talbots, was the seller of the Talbots intangibles; or, in the alternative, if the sale of the Talbots intangibles was compressed by application of the step-transaction doctrine, then that doctrine also required that the Day 1 and Day 2 transactions be reduced to a single transaction for the sale of Talbots stock. One oblique reference to the unitary business principle on page 28 of Petitioners' appellate brief does not constitute a properly presented constitutional claim. Pet. App. 107a-108a (Petition for Rehearing). *See United States v. Zannino*, 895 F.2d 1, 17 (1st Cir. 1990) (documenting "settled appellate rule that issues averted to in a perfunctory manner, unaccompanied by some effort at developed argumentation, are deemed waived"); *Greater Media, Inc. v. Department of Public Utils.*, 415 Mass. 409, 418, 614 N.E.2d 632, 637 (1993) (federal claim stated in conclusory fashion

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clauses. Pet. App. 30a. The Supreme Judicial Court rejected this unsupported claim as "speculative." Pet. App. 30a. In their Petition for a Writ of Certiorari, General Mills and Talbots appear to include the numerator issue as part of their overall constitutional claim involving the step-transaction doctrine. Pet. 15-19. Petitioners argue that the Massachusetts Commissioner's application of the step-transaction doctrine to the Day 1 intangibles sale was unconstitutional because it resulted in a "distortive" state tax, by including the $100 million gain in Talbots's apportionable tax base and the $100 million in gross receipts in the numerator of Talbots's Massachusetts sales factor. Pet. 18-19. The fact that Petitioners raised below a portion of the overall claim that they now seek to present does not mean that the overall claim was preserved for this Court's review.

failed to rise to level of adequate appellate argument and thus was deemed waived under Mass. R.A.P. 16(a)(4)). In sum, this Court lacks jurisdiction over Petitioners' claims because the Supreme Judicial Court was not confronted with and did not address either of the two issues Petitioners now seek to present to this Court. The Petition should be denied for that reason alone.

II. THE PETITION FAILS TO SHOW A CONFLICT IN THE COURTS BELOW OR PRESENT AN ISSUE OF NATIONAL IMPORTANCE THAT MERITS REVIEW BY THIS COURT.

Even assuming that Petitioners' claims are properly before this Court, the Petition should still be denied because it presents no issues meriting this Court's attention. Beyond a conclusory allegation that the decision below presents issues "of utmost importance" to the Court's due process and commerce clause jurisprudence, the only asserted reason for granting the Petition is that "[m]any multistate and multinational taxpayers have gains on the sale of discrete business entities, where the transaction is the subject of an IRC Section 338(h)(10) election." Pet. 12-13. That is an insufficient justification for plenary review.

Petitioners do not claim that the Supreme Judicial Court "has decided an important federal question in a way that conflicts with the decision of another state court of last resort or of a United States court of appeals." *See* Supreme Court Rule 10(b). Petitioners cite no state or federal court of appeals cases relating to their step-transaction claim. Pet. 12-13, 15-19. For the I.R.C. § 338(h)(10) election transaction, Petitioners cite three lower-court state opinions without alleging that those cases even address the constitutional claim

Petitioners now raise.[2] Pet. 12-13, 13-15; *see* Technical Corrections Act of 1982, Pub. L. No. 97-448, § 306(a)(8)(B)(i), 96 Stat. 2365 (1983) (adding deemed-asset sale election to Internal Revenue Code effective 1983).

Furthermore, neither of Petitioners' claims rises to the level of national importance warranting plenary review, for several reasons. First, this case involves facts so unique and complex that Petitioners have resorted to two flow charts to explain their version of the pertinent events. Pet. 4-7. Such a fact-bound case would provide a poor springboard for elaboration of general constitutional principles.

Second, even though Petitioners' constitutional claims were not passed upon below, it is clear that the claims are so bound up with the facts that any decision of this Court in Petitioners' favor would amount to little more than the correction of erroneous factual findings. *See* Supreme Court Rule 10 (plenary review "rarely granted" to correct erroneous factual findings or the misapplication of a properly stated rule of law). While this is true of both of Petitioners' constitutional claims, it applies with particular force to the claim involving the Day 1 sale of the Talbots intangibles, the

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[2] Indeed, in both the *Canteen Corp.* and *Osram Sylvania* cases, the question before the court was simply whether the gain from a deemed sale of assets pursuant to an election under I.R.C. § 338(h)(10) was taxable as business income or nonbusiness income under Pennsylvania law. *See Canteen Corp. v. Pennsylvania*, 818 A.2d 594 (Pa. Commw. Ct. 2003); *Osram Sylvania, Inc. v. Pennsylvania*, No. 310 F.R. 1998, Pa. St. Tax Rep. (CCH) ¶ 203-090 (Pa. Commw. Ct. Mar. 6, 2003). The Pennsylvania appeals court concluded that the gain was reportable by and taxable to the subsidiary as nonbusiness income. *See id.*

transaction that generated most of the disputed tax. Pet. 15-19. The alleged constitutional error was triggered by a Supreme Judicial Court factual finding with which Petitioners disagree: that the Day 1 and Day 2 sales constituted two separate transactions, each of which was independently subject to the step-transaction doctrine.[3] If the Supreme Judicial Court was right that the Day 1 intangibles sale was a distinct transaction, taxing the substance of the transaction -- a sale of intangibles by Talbots, a Massachusetts corporation[4] -- does not even implicate, much less show a violation of, the unitary business principle. *See generally Allied-Signal, Inc. v. Director, Div. of Taxation*, 504 U.S. 768, 780 (1992) (noting that the unitary business principle limits the states' constitutional reach when the taxpayer in question, unlike Talbots, is a non-domiciliary corporation vis-a-vis the taxing state). Similarly, Petitioners' I.R.C. § 338(h)(10) election claim goes nowhere unless it is indeed the case that the election was a federal "fiction" that produced no income in Massachusetts. Pet. 13-15. The Supreme Judicial Court, in addressing Petitioners' state-

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[3] The Supreme Judicial Court said that if it were to collapse the Day 1 and Day 2 sales into a single transaction, it "would be changing the basic nature of [the parties'] agreement," which created, and also presented to the federal government for taxation, two transactions on two different days, involving four distinct corporations. 27a.

[4] Based on the circumstances surrounding the Day 1 sale of the Talbots intangibles -- including the fact that Tal HC was not created until General Mills expressed concern about the sale being subject to Massachusetts tax -- the Supreme Judicial Court concluded that Tal HC had no legitimate role in the intangibles sale other than to avoid Massachusetts tax. 25a-26a.

law claim, rejected that argument as a factual matter.[5]

Finally, this Court should reject Petitioners' attempt to further federalize the step-transaction claim by alleging an error of the federal step-transaction doctrine. Pet. 15-19. The Supreme Judicial Court applied the Massachusetts step-transaction doctrine, and thus could not have "violated" principles set forth in federal cases cited only as persuasive analogies.[6] Pet. App. 24a-27a. While state law may incorporate by reference federal statutes or common-law principles, clearly a state does not actually apply federal law to determine, as a matter of state law, whether state tax is due. In any event, the Supreme Judicial Court correctly applied the doctrine, which is essentially an analytical tool to facilitate the general principle that taxation depends on the substance of a transaction rather than its form. Pet. App. 24a-27a; *see Commissioner of Revenue v. Dupee*, 423 Mass. 617, 624, 670 N.E.2d 173, 178 (1996).

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[5] The Supreme Judicial Court found that the I.R.C. § 338(h)(10) election had very real income-tax consequences that resulted in adjustments during negotiations between General Mills and JCL. 23a. Separately, the court noted that there was no suggestion that following M.G.L. c. 63, § 30 -- which generally makes Massachusetts income the same as federal taxable income -- would cause confusion among the states and lead to double taxation. 23a.

[6] While the fact that the court below applied the Massachusetts step-transaction doctrine does not eliminate Petitioners' federal constitutional claim, it would of course eliminate this Court's jurisdiction over any claim based solely on alleged error in applying the step-transaction doctrine.

III. PETITIONERS' CLAIMS ARE WITHOUT MERIT.

The Petition should also be denied because the constitutional claims are without merit. Petitioners fail to meet their "distinct burden of showing by 'clear and cogent evidence' that [the state tax] results in extraterritorial values being taxed." *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 164 (1983), quoting *Exxon Corp. v. Department of Revenue of Wis.*, 447 U.S. 207, 223 (1980). The Massachusetts apportionment formula need only produce "a 'rough approximation' of the corporate income that is 'reasonably related to the activities conducted within the taxing state.'" *Id.* at 223, quoting *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 273 (1978). The Massachusetts Commissioner assessed tax because Talbots, a Massachusetts corporation with in-state headquarters, management, and operations, sold assets in two separate transactions. That is how the parties chose to structure the sale of Talbots to JCL. Petitioners' argument -- essentially, "do-as-I-say-not-as-I-do" -- falls flat. The Supreme Judicial Court correctly affirmed the decision of the Massachusetts Commissioner assessing state tax on Talbots for the Day 1 intangibles sale and Day 2 deemed-asset sale. Pet. App. 1a-30a.

Conclusion

For all of the reasons stated above, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

THOMAS F. REILLY
Attorney General
Of Massachusetts

Thomas A. Barnico
Counsel of Record
Victoria S. Cole
Assistant Attorneys General
One Ashburton Place
Boston, MA 02108
(617) 727-2200, ext. 2086

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